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**OFFICE OF
INSURANCE COMMISSIONER**

TECHNICAL ASSISTANCE ADVISORY
T 05-08

TO: Property and Casualty Insurers Authorized in Washington

SUBJECT: Rate Filing Simplification

DATE: November 9, 2005

On October 31, 2005, the Washington Office of Insurance Commissioner (OIC) adopted a revised rule that describes how property and casualty insurers must show in their rate filings that their proposed rates comply with the requirements of RCW 48.19.020: Rates must not be excessive, inadequate, or unfairly discriminatory. The revised rule will be effective January 1, 2006.

We believe this revised version of WAC 284-24-065 is written clearly. However, because the newly adopted rule eliminates many of the details that were prescribed in the previous rule, there may be some uncertainty in the insurance industry about how the new rule will be implemented and applied. The purpose of this Technical Assistance Advisory is to reduce this uncertainty and provide some guidance to insurance compliance professionals who prepare and submit property and casualty insurance rate filings in Washington. We will use a question-and-answer format.

What are the major changes in this revision?

The revised rule is much shorter. It contains few details about how to calculate an underwriting profit provision that is consistent with your company's cost of capital. It establishes a range of expected operating ratios, from 0% to 5%, for which proposed rates will not be considered excessive or inadequate. However, it also recognizes that, using accepted ratemaking principles, insurers may be able to support rates for which the expected operating ratio is outside that range.

What stays the same?

The underlying ratemaking principle, taken from the Casualty Actuarial Society's *Statement of Principles Regarding Property and Casualty Insurance Ratemaking*, remains the foundation of this regulation: Rates should be actuarially sound estimates of the expected costs of risk transfer. The revised regulation also retains the definition of *operating ratio* and the requirement that the effect of risk loads in increased limits factors be taken into account.

In which kinds of rate filings should I be concerned about complying with this regulation?

This regulation is relevant only to initial rate filings and rate filings in which you propose revised base rates or a change in your overall rate level for a program. You should not be concerned about complying with the requirements of WAC 284-24-065 if you are filing a rule change or relativity change that has only a minor premium effect. However, you will still need to include supporting information appropriate to that kind of change.

If my company includes rate filing documentation similar to what we provided to OIC under the old rule, will that be acceptable?

Probably. The revised rule still contains the same underlying principles, so the same kind of documentation you have provided in the past may still be appropriate and acceptable. But because many of the details have been deleted from the rule, you may also be able to present less detail in the supporting information for your rate filings.

What will OIC focus on in its review of my company's rate filings?

OIC's rate filing review will focus on your company's proposed rates and whether they are justified by actuarially sound estimates of the expected costs of transferring risk from your policyholders to you. The 0%-to-5% operating ratio window should not lead you to believe that our only interest is in your expected operating ratio. We will continue to review your filing documentation, including actuarial methods, loss development, trend factors, expense estimates, investment income calculations, indicated relativities, etc. We will also continue to emphasize the statutory requirement that your rates not be unfairly discriminatory.

If I calculate the expected operating ratio corresponding to my company's proposed rates to be between 0% and 5%, will my rate filing automatically be approved?

Not automatically. In each rate filing it may be helpful if you show your calculation of the expected operating ratio corresponding to your proposed rates. However, even if that expected operating ratio is between 0% and 5%, your filing does not get a free pass. We will also be reviewing the data and actuarial methods supporting your proposed rates. For example, if you have overestimated your loss trend factors, the expected operating ratio corresponding to your proposed rates may be higher than you thought it was. And as is mentioned above, we will continue to watch for the possibility of unfairly discriminatory rates.

If my company proposes a large rate increase but the expected operating ratio is still less than 0%, will the proposed rates be disapproved as inadequate? Or if we propose a large rate decrease but the expected operating ratio is still greater than 5%, will the proposed rates be disapproved as excessive?

In the rate review process we will continue to be concerned about rate stability. We have no desire to cause market disruptions. As in the past, if you propose to take a sizeable step toward your indicated rate level, we are not likely to consider your proposed rates to be excessive or inadequate.

My company has an approved return-on-equity reference document on file with OIC. Under the revised rule can we still refer to that document? Will return-on-equity reference documents still be accepted?

In 1991, when the provisions of WAC 284-24-065 were first implemented, OIC recognized that compliance with new, detailed regulations pertaining to cost-of-capital calculations would be difficult for some insurers. OIC's acceptance of return-on-equity reference documents was a way to make the process easier for some insurance compliance professionals. Now that most of the detailed requirements have been removed from the regulation, return-on-equity reference documents are no longer needed and will not be accepted. Each rate filing should include its own documentation and should not refer to or depend on an approved return-on-equity reference document. If your rate filings still include cost-of-capital calculations, we recommend that you develop an efficient, concise way to present this information. (We do not want to see your 200-page fair-rate-of-return study in every rate filing!) Of course, if you are filing rates for various programs or lines of business, it is still important to maintain consistency with respect to your company's target after-tax rate of return on equity and its allocation of surplus.

Do I still need to include OIC's required form, the Return on Equity Worksheet, in every rate filing?

No. The Return on Equity Worksheet is being discontinued, and it will not be replaced by any other required form.

If you have questions regarding this Technical Assistance Advisory, you may contact OIC's Senior Actuary, Lee Barclay, at (360) 725-7115 or LeeB@oic.wa.gov.